KCC Talgaon Kalmath Highways Private Limited

September 19, 2022

Rating

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	192.89 (Enhanced from 160.66)	CARE AA+; Stable (Double A Plus; Outlook: Stable)	Revised from CARE AA-; Stable (Double A Minus; Outlook: Stable)
Total bank facilities	**192.89 (₹ One hundred ninety-two crore and eighty-nine lakh only)**		

Details of instruments/facilities in Annexure-1.

Detailed rationale and key rating drivers

The revision in the rating assigned to the bank facilities of KCC Talgaon Kalmath Highways Private Limited (KTKHPL) takes into account the completion of the entire work on the project stretch thereby eliminating the residual implementation risk and receipt of final commercial operations date (COD) with effect from September 27, 2021. The rating revision further factors in the successful receipt of five full annuities from Ministry of Road Transport and Highways (MoRTH) including the balance differential amount towards first three annuities, which were earlier not fully paid due to non-completion of the works on the entire stretch and reduction in the interest rate post refinancing of project term loan. Given the repo rate-linked structure for the refinanced loan, interest rate risk is expected to be substantially mitigated.

The rating also favourably factors KTKHPL's low project leverage post, refinancing and minimal counterparty credit risk associated with MoRTH as the annuity provider. Various liquidity support mechanisms including debt service reserve account (DSRA) equivalent to six months of debt servicing requirements, creation of major maintenance reserve account (MMRA) and the inherent strengths of hybrid annuity model (HAM) are other credit positives for KTKHPL.

The above rating strengths are partially offset by the inherent operation and maintenance (O&M) and interest rate risk. Relatively lower level of provision of MMRA vis-à-vis other similar projects may dilute cash flow resilience in the year of major maintenance. Nevertheless, experienced sponsor- KCC Buildcon Private Limited (KBPL), in operating and maintaining similar road assets are expected to mitigate the risk to an extent.

The rating also takes note of the put option exercisable at the end of five years against the notice period of 90 days thus exposing KTKHPL to refinancing risk. Nevertheless, strong credit profile of the counterparty, adequate tail period, established track record of annuity receipts and low project leverage of around 39% post refinancing mitigate the refinancing risk to a large extent.

Rating sensitivities

Positive factors – Factors that could lead to positive rating action/ upgrade:

- Enhancement in MMRA built up leading to superior cash flow resilience on sustained basis.

Negative factors – Factors that could lead to negative rating action/ downgrade:

- Deterioration in the credit risk profile of the counterparty.
- Non-compliance with maintenance obligation as specified in the Concession Agreement leading to delay/ deduction in annuities.
- Any adverse movement in O&M expenses or interest rate affecting the debt coverage parameters below 1.10.
- Non-adherence to sanctioned debt terms.
- Additional debt availed by the company thereby moderating its coverage indicators

Detailed description of the key rating drivers

Key rating strengths

Achievement of final COD and receipt of five annuities: The project achieved provisional commercial operation date (PCOD) for 29.160 km of the project stretch (75.97% of the total length of 38.38 km) on December 14, 2019. On account of the pending receipt of final COD, the company had received first annuity to the tune of 90% and second and third annuities to the tune of 97% each.

Post the completion of the works on the entire stretch, the company received the final COD with effect from September 27, 2021. Balance construction works of around 150m, which do not correspond to the main carriageway and for which the land has not yet been awarded by the Authority shall be completed by the engineering, procurement and construction (EPC) contractor, i.e., KBPL, as and when the said land is made available by the Authority, out of its own sources without impacting the cash flows of the project. The company is now receiving 100% of the annuities due without any deductions and has also received the balance differential amounts towards first three annuities; along with full amounts towards fourth and fifth annuities.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

Cash flow visibility due to annuity nature of the revenue stream linked to inflation inflation-indexed bid project cost (BPC) as well as O&M annuity and bank rate linked interest annuity: During the operational phase, cash flow is assured in the form of annuity payments from MoRTH on semi-annual basis covering 60% of the project completion cost along with interest at 'bank rate plus 3%' on reducing balance and inflation-indexed O&M annuity.

Low counterparty credit risk: MoRTH is an apex organisation under the Central Government, is entrusted with the task of formulating and administering, in consultation with other Central Ministries / Departments, State Governments / UT Administrations, organisations and individuals, policies for Road Transport, National Highways and Transport Research with a view to increasing the mobility and efficiency of the road transport system in the country. The outlook on MoRTH reflects the outlook on the sovereign, whose direct and indirect support continues to be the key rating driver.

Mitigation of interest rate risk to a large extent: In February 2022, the company has refinanced the existing term loan with a new term loan. In addition, the company has also availed a top-up loan, which has been utilised for the purpose of retiring the unsecured loans brought in by the sponsor as part of the project cost during the project implementation phase. The refinanced loan has now been linked with the repo rate, with right to reset the interest rate spread annually, subject to step-up events as per the terms of sanction. Given the stability of the cash flow due to repo rate linked structure, interest rate risk is expected to be substantially mitigated. This combined with tail period of one and a half year, thereby leaving three semi-annuities, is viewed favourably.
Moreover, as per the sanction terms, the company is maintaining DSRA equivalent to six months of debt servicing requirements, which shall be maintained throughout the tenor of the debt.

Key rating weaknesses
Inherent O&M risk associated with the project: Close to 66% of KTKHPL carriageway is rigid pavement and balance is flexible. While the inflation-indexed O&M annuity partly mitigates O&M risk, the disparate movement in inflation index (70% WPI; 30% CPI) and the O&M cost heads poses a risk. Besides, the company could face the risk of a sharp increase in the O&M cost in the event wear and tear on the road is more-than-envisaged.
KTKHPL is maintaining a MMRA out of the project cash flow to conduct the MM on the project stretch as per stipulated sanctioned terms. The company has already created MMRA reserve of ₹5.62 crore (in the form of fixed deposits) as on July 20, 2022. CARE Ratings notes that O&M as well as MM assumptions for KTKHPL are relatively lower as compared to its peers.
Relatively lower level of provision of MMRA vis-à-vis other similar projects may dilute cash flow resilience in the year of major maintenance. Nevertheless, low leverage and track record of sponsor in operating roads offer some credit strengths.

Put option of term loan: The refinanced debt has a put option exercisable at the end of five years against a notice period of 90 days thus exposing KTKHPL to refinancing risk. However, strong credit profile of counterparty, adequate project leverage and timely receipt of annuity mitigates the refinancing risk to a large extent.

Liquidity: Strong
KTKHPL is envisaged to generate healthy cash flows backed by a steady revenue stream in form of annuity payments throughout the tenor of the term loan. Furthermore, there is a gap of around 50 days between the scheduled annuity payment date and the debt repayment date, which provides an additional cushion in case of a delay in receipt of the annuity. As on July 20, 2022, the company is maintaining DSRA of ₹13.25 crore in the form if fixed deposits (FDs), which is equivalent to six months of debt servicing and MMRA reserve of ₹5.62 crore in the form of FDs. In addition, the company is also maintaining unencumbered FDs to the tune of ₹7.55 crore to take care of interest servicing and operational expenses till the receipt of next annuity.

Analytical approach: Standalone

Applicable criteria
Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Financial Ratios – Non-Financial Sector
Rating Methodology - HAM Road Projects
Liquidity Analysis of Non-Financial Sector entities

About the Company
KTKHPL, a special purpose vehicle (SPV), incorporated and owned by KBPL, has entered into 15-year concession agreement (CA), excluding construction period of 730 days, with MoRTH for the design, build, operate and transfer (DBOT) through Public Works Departments, Govt. of Maharashtra for rehabilitation and up-gradation of Talgaon to Kalmath section from km 367.200 to km 406.030 of NH-66 (erstwhile NH-17) to 4-lane with paved shoulder (length: 38.38 km) in the state of Maharashtra under NHDP –IV on hybrid annuity mode.
The project achieved the appointed date on December 04, 2017, while the PCOD was achieved on December 14, 2019, and final COD on September 27, 2021. The company has received five annuities during the operational period.

Brief Financials- Standalone (₹ crore)	FY21 (A)	FY22 (Prov.)	Q1FY23 (UA)
Total operating income	49.26	70.36	NA
PBILDT	21.33	21.32	NA
PAT	5.50	8.21	NA
Overall gearing (times)	2.55	7.08	NA
Interest coverage (times)	1.36	1.47	NA

A: Audited; Prov.; Provisional; NA: Not available
Note: The financials are classified as per CARE Ratings' internal standards.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history (Last three years): Please refer Annexure-2

Covenants of rated instruments/facilities: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Term loan	NA	-	-	Jul-2033	192.89	CARE AA+; Stable

NA: Not Applicable

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Fund-based - LT-Term loan	LT	192.89	CARE AA+; Stable	-	1)CARE AA-; Stable (01-Oct-21) 2)CARE AA-; Stable (30-Aug-21)	1)CARE A-; Positive (17-Sep-20)	1)CARE A-; Stable (02-Jul-19)

*Long term/Short term.

Annexure-3: Detailed explanation of covenants of the rated instruments/facilities

Long-term loan	Detailed explanation
A. Financial covenants	• DSCR of at least 1.15x for the tenor of facility
B. Non-Financial Covenants	• During the currency of the lender's credit facilities, the borrower shall not, without prior approval of the lenders in writing effect any change in the capital structure other than as contemplated in the arrangement. • All equity, quasi equity, equity like instruments and subordinated debt shall be subordinated to the facility, including in terms of security, tenor and rights relating to acceleration, payments related to coupon, interest, dividend and redemption under these instruments shall be permitted only from the distribution of residual amounts in terms of the usage of revenue provided and in accordance with the restricted payment conditions as stipulated by the lenders.

Annexure-4: Complexity level of various instruments rated for this company

Sr. No.	Name of Instrument	Complexity Level
1	Fund-based - LT-Term loan	Simple

Annexure-5: Bank lender details for this company

To view the lender-wise details of bank facilities please click here

Note on complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

Contact us

Media contact
Name: Mradul Mishra
Phone: +91-22-6754 3596
E-mail: mradul.mishra@careedge.in

Analyst contact
Name: Harish Kumar Chellani
Phone: +91-22-6837 4472
E-mail: harish.chellani@careedge.in

Relationship contact
Name: Swati Agrawal
Phone: +91-11-45333237
E-mail: swati.agrawal@careedge.in

About us:
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